



**COUNTY OF LOS ANGELES  
DEPARTMENT OF AUDITOR-CONTROLLER**

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WENDY L. WATANABE  
AUDITOR-CONTROLLER

September 19, 2013

TO: Marvin J. Southard, D.S.W., Director  
Department of Mental Health

FROM: Wendy L. Watanabe  
Auditor-Controller

A handwritten signature in blue ink, reading "Wendy L. Watanabe", is written over the printed name of the Auditor-Controller.

SUBJECT: **DEPARTMENT OF MENTAL HEALTH – REVIEW OF TRUST FUNDS  
AND REVENUE ACCRUALS**

As part of our ongoing responsibility to ensure the County's resources are safeguarded and that departments comply with County fiscal policy and procedures, we are reviewing County departments' use of trust funds. Our reviews are intended to ensure departments are controlling and using trust funds in compliance with the County Fiscal Manual (CFM) and other requirements.

We have performed a limited review of the Department of Mental Health's (DMH or Department) trust funds and revenue accruals relating to the trust funds. Our review included interviews with DMH management and staff, and tests of DMH's records.

Based on our review, it appears that DMH uses trust funds for the intended purpose. However, we noted that DMH needed to replace one trust fund with a general fund liability account. In addition, DMH should evaluate the Department's revenue recognition procedures to determine if the Department can recognize revenue from trust funds more timely, and should ensure staff adequately document trust fund reconciliations. DMH should implement alternative strategies to obtain responses to requests for Medi-Cal accounts receivable confirmations, and review and maintain adequate supporting documentation for year-end revenue accruals. The following are detailed results of our review and recommendations.

**Trust Funds/General Fund Liability Accounts**

Departments use trust funds for a number of purposes, including temporarily holding funds that belong to other parties, and holding revenue until it is earned and/or allocated

to the appropriate entities/accounts. Departments use liability accounts in the County's general fund to record obligations such as amounts they owe. General fund liability accounts may also be used to record obligations to provide goods/services for revenue received but not yet earned.

DMH currently has three trust funds and two general fund liability accounts with a total balance of \$80.5 million as of June 30, 2012. The Department primarily uses its trust funds/accounts to temporarily hold incoming payments and fees, court-ordered settlements, and donations until they are recognized as revenue or transferred to the proper account. We included the general fund liability accounts in our review because they function like trust funds, since DMH temporarily holds payments in the accounts until the department determines what amount has been earned and recognizes the associated revenue.

We reviewed DMH's controls over the Federal Funding Participation Trust Fund TL3-3301 (FFP trust fund) and Advances Payable A01-2574 General Fund Liability Account (Advances Payable account), which collectively comprised 99% of DMH's \$41.1 million trust fund balances as of June 30, 2009. We noted the following:

- DMH established the FFP trust fund to receive and hold federal reimbursements for services provided by DMH-operated and contract clinics. The monies received remain in the trust fund until DMH calculates the appropriate amount to recognize as revenue. DMH's practice of holding monies in the FFP trust fund negatively impacts the County's cash flow position because these monies are not available for the County to use until DMH transfers them to revenue.

Based on our review of DMH's documentation of the FFP trust fund's purpose and authority, it appears that DMH is not required to hold federal reimbursements in a trust fund. Therefore, the Department should establish a general fund liability account to temporarily hold federal reimbursements instead of using the FFP trust fund. Using a liability account will maintain DMH's ability to track monies received while improving cash flow.

Subsequent to our review, the Department informed us that they worked with the Auditor-Controller's Accounting Division to close the FFP trust fund, and established a new general fund liability account, as recommended.

- As of June 30, 2009, the FFP trust fund and Advances Payable account had balances of \$23.7 million and \$16.9 million, respectively. According to DMH management, some of the year-end balances were revenue that DMH had not yet earned (e.g., overpayments from the State). However, we noted that some of the monies had been in the trust fund/account for over two years, which indicates that there may have been a significant lapse of time between the period when revenue was earned and the period it was recognized. Delays in the recognition of revenue

impact the accuracy of the County's financial records. DMH needs to evaluate its revenue recognition procedures to determine if the Department can recognize revenue from trust funds/accounts more timely, particularly within the fiscal year the revenue is earned.

- CFM Section 2.3.0 requires departments to reconcile trust funds to the County's official accounting records (eCAPS) monthly, or quarterly if the fund balance is less than \$5,000. The reconciliations should be documented and approved by a supervisor or manager who has no other trust fund responsibilities. Because the Advances Payable account functions like a trust fund, DMH should ensure that applicable trust fund controls are followed for this account. We noted that DMH's reconciliations for the Advances Payable account and the FFP trust fund did not specify the source of numbers used for the reconciliations. Therefore, it was unclear if DMH's internal records were being reconciled to eCAPS. In addition, there was no documentation that a supervisor approved the reconciliations. DMH needs to ensure reconciliations are properly documented.

### **Recommendations**

#### **DMH management:**

- 1. Replace the FFP trust fund with a general fund liability account.**
- 2. Evaluate revenue recognition procedures to determine if the Department can recognize revenue from trust funds more timely, particularly within the fiscal year the revenue is earned.**
- 3. Ensure reconciliations for trust funds/general fund liability accounts are properly documented to include the sources used to perform the reconciliations and the approver's signature.**

### **Accounts Receivable**

CFM Section 9.1.6 requires departments to establish accounts receivable at year-end for revenue earned during the fiscal year but not yet received. These receivables should be accrued only if they are earned, measurable, and expected to be received within 12 months of the end of the current fiscal year. At the end of Fiscal Year 2008-09, DMH reported approximately \$430 million in accounts receivable. DMH's receivables primarily relate to Medi-Cal programs.

We reviewed the Department's methodology for calculating accounts receivable and noted the following:

- DMH's Accounting Division routinely sends to the State requests for confirmation of Medi-Cal amounts due. These confirmations provide assurance that the State agrees with the receivables that DMH records at year-end. However, the State has not responded to DMH's confirmation requests. Because the amounts involved are significant and affect the County's revenue and cash flow projections, DMH should develop alternative strategies to obtain confirmation of Medi-Cal receivables from the State.
- As noted above, departments should only record accounts receivable for amounts that have been earned and are expected to be received during the subsequent fiscal year. If the amounts are not expected to be received within the next fiscal year, departments may need to record long-term receivables. We noted that DMH does not typically receive all recorded accounts receivable within 12 months. This negatively impacts the County's cash flow position, because accounts receivable are anticipated to be available to provide cash for current operational expenses. Prior to each fiscal year end, DMH management should develop methods to more accurately determine the anticipated timing of their receipt of accounts receivable, and record receivable amounts accordingly.
- As noted above, Medi-Cal reimbursements comprise the majority of the Department's year-end accounts receivable. A DMH manager performs complex calculations to determine how much Medi-Cal accounts receivable DMH should accrue. We noted that the calculations are not reviewed or verified by DMH management. In addition, the Department does not have desk procedures for calculating year-end receivables. DMH management needs to review and verify accounts receivable calculations. DMH management should also develop written procedures for calculating year-end receivables to ensure operational continuity.
- We reviewed DMH's calculation for accounts receivable for the fiscal year ended June 30, 2009. DMH estimates its Medi-Cal receivables based on reports the Department generates from the State's Medi-Cal system. DMH did not retain copies of the reports used to calculate receivables. Because the Medi-Cal system does not maintain historical balances, we were unable to verify that DMH used the appropriate data to calculate Medi-Cal receivables. DMH needs to ensure that staff calculating accounts receivable maintain adequate supporting documentation, including Medi-Cal reports used for calculations.

#### **Recommendations**

##### **DMH management:**

- 4. Develop alternative strategies to obtain confirmation of Medi-Cal receivables from the State.**

- 5. Develop methods to more accurately determine the anticipated timing of their receipt of accounts receivable, and record receivable amounts accordingly.**
- 6. Review and verify accounts receivable calculations, and develop written procedures for calculating year-end receivables to ensure operational continuity.**
- 7. Ensure that staff calculating accounts receivable maintain adequate supporting documentation, including Medi-Cal reports used for the calculations.**

#### **Review of Report**

We discussed the results of our review with DMH management. The Department's attached response indicates agreement with our findings and recommendations.

We thank DMH management and staff for their cooperation and assistance throughout our review. Please call me if you have any questions, or your staff may contact Robert Smythe at (213) 253-0101.

WLW:RS:TK

Attachment

c: Robin Kay, Chief Deputy Director, DMH  
Audit Committee



LOS ANGELES COUNTY DEPARTMENT OF MENTAL HEALTH  
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Reply To: (213) 738-4601 Fax: (213) 386-1297



MARVIN J. SOUTHARD, D.S.W.  
Director  
ROBIN KAY, Ph.D.  
Chief Deputy Director  
RODERICK SHANER, M.D.  
Medical Director

August 15, 2013

Via Electronic Mail

Wendy L. Watanabe, Auditor-Controller  
Department of Auditor-Controller  
Kenneth Hahn Hall of Administration  
500 West Temple Street – Room 525  
Los Angeles, CA 90012-3873

Dear Ms. Watanabe:

**DEPARTMENT OF MENTAL HEALTH – REVIEW OF  
TRUST FUNDS AND REVENUE ACCRUALS**

This is in response to your recent limited review of the Department of Mental Health's (DMH) trust funds and revenue accruals relating to the trust funds. On Thursday, May 9, 2013, Carrie Guo of your staff had a telephone conversation with Mike Motodani, Chief, Accounting Division, to review the findings and recommendations.

Based upon the information discussed and the exchange of additional information provided, this is confirmation that DMH concurs with the findings of your limited review.

If you have any questions or need additional information, please contact me at (213) 738-4601, or your staff may contact Kimberly Nall, Finance Manager at, (213) 738-4625.

Sincerely,

Marvin J. Southard, D.S.W.  
Director

MJS:KN

c: Robin Kay  
Margo Morales  
Kimberly Nall